

CHAPTER 7. INVESTMENT CLIMATE

OPENNESS TO FOREIGN INVESTMENT

The Royal Thai Government (RTG) has long maintained an open, market-oriented economy and encouraged foreign direct investment as a means of promoting economic development, employment, and technology transfer. Thailand welcomes investment from all countries and seeks to avoid dependence on any one country.

In the wake of the 1997 Asian Financial Crisis, the Thai government in concert with the International Monetary Fund (IMF) has embarked on an economic reform program intended, in part, to foster a more competitive and transparent climate for foreign investors and creditors in an effort to stimulate investment flows. Many aspects of the reform measures enacted after the crisis were controversial, and were resisted strongly by the political opposition and other powerful elements of Thai society. Despite some setbacks, however, the reform process is continuing.

The primary focus of the RTG reform program has been the financial sector, which was crippled by a huge amount of bad debt resulting from the financial crisis. Legislation establishing a new bankruptcy court, reforming bankruptcy and foreclosure procedures, and allowing creditors to pursue payment from loan guarantors has been enacted. Other reforms include amendments to the Land Code, the Condominium Act, and the Property Leasing Act, all of which will liberalize, to some extent, restrictions on property ownership by non-Thais.

The new Alien Business Act became law in early 2000, replacing the old Alien Business Law of 1972 (National Executive Council Announcement No. 281). The new law governs most investment activity by non-U.S. nationals, opens additional sectors to foreign investment, and increases maximum ownership stakes permitted in some sectors above the current 49 percent limitation. As of July 2001, the ministerial regulations guiding the Act's implementation are still under review, but are expected to be implemented by the end of 2001.

Pledging to spur economic recovery through a revival in domestic economic capacity and demand, a new government led by Prime Minister Thaksin Shinawatra took office early in 2001. Despite the new government's emphasis on domestic sources of economic growth, Thailand remains committed to economic reform and an open investment climate.

TREATY OF AMITY

The U.S.-Thai Treaty of Amity and Economic Relations of 1966 allows U.S. citizens and businesses incorporated in the U.S., or in Thailand that are majority-owned by U.S. citizens, to engage in business on the same basis as Thais, exempting them from most of the restrictions on foreign investment imposed by the Alien Business Law of 1972 (and the 2000 Alien Business Act). Under the Treaty, Thailand restricts American

investment only in the fields of communications, transport, fiduciary functions, banking involving depository functions, the exploitation of land or other natural resources, and domestic trade in agricultural products. Notwithstanding their treaty rights, many Americans choose to form joint ventures with Thai partners, allowing them to hold the majority stake because of their familiarity with the Thai economy and local regulations.

In the Uruguay Round trade negotiations, all parties agreed that the privileges provided by the Treaty of Amity to U.S. investors in the service sector would be exempted from "Most Favored Nation" (MFN) requirement for ten years, beginning with the establishment of the World Trade Organization (WTO) in January 1995. During this ten-year period, Thailand is expected to liberalize its investment regime so as to provide roughly equivalent treatment to all foreign investors in the service sector. If treatment for all foreign investors is not equal to that provided under the Treaty of Amity by 2005, the Treaty will have to be adjusted or another exemption sought.

REGISTRATION, WORK PERMITS

Any entity wishing to do business in Thailand must register with the Department of Commercial Registration in the Ministry of Commerce. Firms engaging in production activities need to register with the Ministries of Industry and Labor. American citizens can enter Thailand without a visa for visits of up to thirty days. In order to apply for a work permit, a foreigner must enter Thailand on a non-immigrant visa (issued at Thai embassies and consulates) for a stay of three months or, for foreigners with well-defined work or business plans, for a stay of one year. Issuance of the three-month visa usually is completed within two or three days; the one-year visa requires approval from the Immigration Bureau of the Thai Police Department in Bangkok. Upon obtaining a work permit, a holder of a three-month visa may apply for a one-year visa, which generally can be extended every year. Foreigners holding non-immigrant visas who have lived in Thailand for at least three consecutive years may apply for permanent residence in Thailand if they meet strict criteria regarding investment or professional skills.

The Alien Occupation Law of 1972 (decree no. 322) lists occupations reserved exclusively for Thais, which include professional services such as accounting, architecture, law, and engineering, the manufacture of traditional Thai handicrafts, and manual labor. The law also states that all non-Thais working in Thailand, with limited exceptions, must possess a work permit issued at the discretion of the Ministry of Labor and Social Welfare, although some foreigners already working in Thailand were exempted through a "grandfather" clause. Factors that influence the granting of work permits include the degree of specialization required by the position; the size of the firm in terms of number of employees and registered capitalization; and the ratio of Thai nationals to foreigners employed by the firm. Foreigners working for the Thai government or working for projects promoted by the Board of Investment usually have little difficulty obtaining work permits. Work permits in other areas are sometimes difficult to obtain, despite the fact that senior managers and technical personnel are in short supply.

LAND OWNERSHIP

In general, non-Thai business and citizens are not permitted to own land in Thailand unless the land is on government-approved industrial estates. Under the recently approved amendment to the Land Code, foreign investors, who invest a minimum of 40 million Baht (just under USD 1 million), will be permitted to buy up to 1,600 square meters of land for residential use with permission of the Ministry of Interior. Petroleum concessionaires may own land necessary for their activities. Many foreign businesses instead sign long-term leases, and then construct buildings on the leased land. Under the newly enacted Property Leasing Bill, non-Thais are allowed to own up to 100 percent of a condominium building, though other restrictions apply. Americans planning to invest in Thailand are recommended to obtain qualified legal advice. Legal advice is particularly important, as Thai business regulations are governed predominantly by criminal rather than civil law. Violation of Thai business regulations can carry heavy criminal penalties, and criminal liability can be assessed under numerous different laws.

PRIVATIZATION

As part of its economic reform program, the Thai Government has embarked on a privatization program for state economic enterprises and state monopolies with the aim of encouraging capital inflows and relieving resource constraints in many key sectors of the economy. State-owned enterprises in Thailand operate primarily in the utility, energy, telecommunications, banking, tobacco, and transportation sectors. In 2000, state enterprises had total revenues of around USD 26.3 billion, employed over 262,000 people, and accounted for around 21.6 percent of Gross Domestic Product (GDP).

In September 1998, the cabinet approved a "Master Plan for State Enterprise Reform". The Master Plan lays out a comprehensive strategy and timetable for privatization in infrastructure, as well as various other state-owned enterprises. A new State Enterprise Corporatization Act, which provides the legal framework for the conversion of state enterprises into stock companies, came into force in December 1999. Corporatization is viewed as an intermediate step toward privatization, but major state enterprises have yet to be converted.

The new Thaksin government has stated its intention to increase the pace of state enterprise privatization. Draft legislation for a National Enterprise Holding Corporation (NEHC) is designed to set up a supervisory entity for state enterprise privatization. The NEHC, which will be 100 percent owned by the Ministry of Finance, will regulate state enterprises that have been converted into private companies under the 1999 State Enterprise Corporatization Act. The draft NEHC bill was slated to go under parliamentary review in August 2001.

The government sees state enterprise privatization as the main means of increasing Thailand's stock market capitalization. As a result, sixteen state enterprises are scheduled to be listed on the stock market between 2001 and 2003. Internet Thailand, the Petroleum Authority of Thailand, and the Joint Telecommunications Company (a

joint venture to be established between the Telephone Organization of Thailand and the Communication Authority of Thailand) plan to offer public shares by the end of 2001. Thai Airways International is slated to offer 400 million shares to public and strategic partners, including 300 million new shares and 100 million shares from the Ministry of Finance's current holdings. Overall, the Ministry plans to reduce its holding from the current 93 percent to 70 percent. Other near-term candidates for public stock offerings include the Telephone Organization of Thailand, the Communication Authority of Thailand, and the tobacco monopoly.

Despite the stated plans, almost no significant privatizations have occurred except in the banking sector, where 75 percent stakes in four banks have been sold to foreign investors. Thailand has removed tax disincentives and lifted a number of regulations on foreign ownership of domestic financial institutions. The previous foreign ownership limit of 25 percent has been raised to 49 percent, and foreign investors will be allowed to own majority shares of financial institutions for a period of ten years. Restrictions on the operations of foreign banks have also eased over the years. Although foreign banks are still limited to operation of a single branch, this stipulation does not significantly hamper operations (foreign banks have access to local ATM pools, for example). Thus, with the exception of the banking sector, there is insufficient basis to comment on how foreign investors will be treated under the program. However, private sector management consultants retained by privatization authorities have indicated that there will be a substantial role for foreign investors in future privatizations.

CONVERSION AND TRANSFER POLICIES

Exchange controls are governed by the Exchange Control Act of 1942, administered by the Bank of Thailand (BOT; Thailand's central bank). Inward remittances are free of controls. The proceeds of exports with a value of more than 0.5 million Baht (around USD 11,000) must be remitted as soon as received and within 120 days of export, and deposited within seven days of receipt.

Commercial banks are authorized to undertake most routine foreign remittance transactions without prior approval of the Bank of Thailand. Thai nationals are subject to quantitative limits on the amount of foreign currency that can be remitted abroad without specific permission of the Bank of Thailand. The limits vary depending upon the purpose of the transaction and range from USD 10 million per annum for business investment or loans to subsidiaries to USD 100,000 for remittances to family members.

All remittances exceeding USD 5,000 for any purpose other than export must be reported to the Bank of Thailand.

EXPROPRIATION AND COMPENSATION

Private property can be expropriated for public purposes in accordance with Thai law, which provides for due process and compensation. In practice, this process is seldom used, and has been principally confined to real estate owned by Thai nationals

and needed for public works projects. U.S. firms have not reported any problems with property appropriation in Thailand. We are not aware of any pending changes in government policies that would adversely affect the property rights of U.S. nationals in this country.

DISPUTE SETTLEMENT

Thailand has a civil and commercial code and a bankruptcy law, amended in 1998. Monetary judgements are made in Baht; foreign currencies in judgements are calculated at the market exchange rate. Decisions of foreign courts are not accepted or enforceable in Thai courts. Disputes such as the enforcement of property or contract rights have generally been resolved through the Thai courts. Thailand has an independent judiciary that generally is effective in enforcing property and contractual rights, but in practice the legal process is slow and litigants or third parties sometimes may affect judgements through extra-legal means. In addition, companies may establish their own arbitration agreements. At present, Thailand is not a member of the International Center for the Settlement of Investment Disputes. However, Thailand is a member of the New York Convention, and enacted its own rules on conciliation and arbitration in the Arbitration Act of 1987. The Arbitration Office of the Thai Ministry of Justice administers these procedures.

The Bankruptcy Act was amended in April of 1998 to provide Chapter 11-style protection to debtors and to give debtors and creditors the option of negotiating a reorganization plan through the courts instead of forcing liquidation. It allowed creditors to extend additional loans to insolvent firms without losing the right to claim compensation during a future restructuring or liquidation process (but only if the new loan is intended to keep the firm operation). The Bankruptcy Act was further amended in 1999 to address some remaining problems and to facilitate the financial restructuring process. New higher minimum levels for individual and corporate bankruptcies were established, and the previous ten-year period of bankruptcy status was reduced to three years. The 1999 amendments went into effect in April 1999.

Amendments to the Civil Procedure Code on Execution of Judgements entered into force in May 1999 and limit appeal options available to debtors in an effort to quicken the foreclosure process. Under the old law, debtors were free to appeal each action taken with respect to the execution of a bankruptcy judgement. Such appeals, often frivolous in nature, were one of the tactics debtors used to delay the foreclosure process.

The Bankruptcy Court Act established a specialized court for bankruptcy cases. Lawmakers hope that this court will develop expertise in corporate restructuring that will speed up the process and help financially weak companies survive. The court began operation in June 1999, and experience thus far has been positive.

PERFORMANCE REQUIREMENTS/INCENTIVES

In its December 1999 remarks on Thailand, the WTO's Trade Policy Review Body noted that Thailand has committed to implement all WTO agreements, including TRIMS.

The Board of Investment (BOI), established by the Investment Promotion Act of 1977, is Thailand's central investment promotion authority. The BOI lists five priority sectors (detailed below), covering hundreds of types of businesses, eligible for investment incentives. Incentives have been suspended in many sectors in which the BOI believes there is no need to encourage further investment, such as the production of canned tuna for export. Generally, the most generous incentives are offered to those economic activities that bring new technology to Thailand and locate investment in less-developed provinces. BOI incentives are of two basic types: tax-based (including tax holidays and tariff exemptions) and non-tax privileges (guarantees, special permissions, services, etc.).

The BOI's overall investment policy, effective from August 1, 2000, is as follows:

1. In order to maximize the benefits of investment to the country and in line with policies supporting good governance, the BOI has moved to improve the efficiency of promotion incentives by introducing a performance-based system that will require promoted investors to submit evidence of compliance with the conditions of their approval in order to claim the benefits of their incentives.
2. To increase the global competitiveness of Thai exports, projects investing 10 million Baht (about USD 200,000) or more (excluding the cost of land and working capital) will be required to obtain international standards certification, such as International Standards Organization (ISO) 9000.
3. In order to ensure that Thai investment policy is in line with all international obligations, the BOI has lifted all local content and export requirements.
4. To encourage the distribution of opportunities and prosperity to the least-developed provinces, the BOI policy of decentralization will continue. Projects locating in the least-developed provinces will receive maximum incentives. These provinces consist primarily of provinces in which average per capita income has been below 85 percent of the national average during the past three years. These provinces include Sisaket, Nong Bua Lamphu, Surin, Yasothon, Maha Sarakham, Nakhon Phanom, Roi-Et, Kalasin, Sakon Nakhon, Buri Ram, Amnat Charoen, Phrae, Phayao, Nan, Satun, Pattani, Yala, and Narathiwat.
5. To support the development of small- and medium-sized enterprises, the minimum investment amount shall remain at one million Baht (approximately USD 22,000), excluding the cost of land and working capital.

6. To promote investment in key sectors, five priority activities have been identified:

- a. Agriculture and agricultural products;
- b. Environmental protection and/or restoration;
- c. Direct involvement in technological and human resource development;
- d. Basic transportation, infrastructure and services; and
- e. Targeted industries

In 1993, the BOI initiated a major shift in emphasis from export orientation to industrial decentralization as a major policy goal. Intended to spur development in rural areas where the population is employed primarily in the labor-intensive agricultural sector, this decentralization focus continues under the new policy. A chief objective is to reduce congestion in the already-overcrowded capital and to strengthen and diversify the economic base in the provinces.

Board of Investment incentives includes:

- Tax Incentives: exemptions/reductions of import duties on imported machinery; reductions of import duties on imported raw materials and components; exemptions from corporate income taxes for three to eight years; and, deductions from net income of infrastructure costs.
- Permissions: to bring in foreign nationals to undertake investment feasibility studies; to bring in foreign technicians and experts to work under promoted projects; to own land for carrying out promoted activities.
- Guarantees: against nationalization; against competition by new state enterprises; against state monopolization of the sale of products similar to those produced by promoted firms; against price controls; against tax exempt import by government agencies or state enterprises of competitive products; and, of permission to export.

BOI benefits that offer the greatest advantage over non-promoted industries are the tax incentives, though their relative value has declined in recent years with the general reduction of import duties and elimination of the former business tax system. The Value Added Tax (VAT) Law, which eliminated the business tax system, has no provision for the BOI to offer VAT exemptions or reductions.

Investors must submit an application form along with supporting documentation to be considered for incentives. In most cases, the BOI decides within sixty days whether or not a project is eligible for investment privileges. BOI policy is to complete action on applications for projects valued in excess of 200 million Baht (USD 4.4 million) within ninety days.

As noted above, the following revisions to the BOI investment promotion scheme became effective on August 1, 2000:

- For projects in the manufacturing sector, majority or total foreign ownership is permitted in any zone.
- The maximum allowable debt-to-equity ratio will be reduced from 4:1 to 3:1.
- Except for the electronic and agriculture industries, projects investing less than 500 million Baht (USD 11 million) must produce added value equal to at least 30 percent of sales revenue.
- For projects of more than 500 million Baht (USD 11 million), a feasibility study must be presented at the time of application.
- The BOI will continue to promote relocation of projects to Zone 2 and Zone 3 (special groupings of 12 and 58 provinces, respectively). However, in order to be eligible for new incentives, projects must relocate to an industrial estate.
- Due to increased levels of development, the provinces of Phuket and Rayong have been moved into Investment Promotion Zone 2, which offers a three-year income tax holiday for promoted projects, unless projects are located in an industrial estate, in which case they receive a five-year investment tax holiday.
- Projects submitted before December 30, 2004 that locate in Zone 2 industrial estates approved by the BOI before the date of the announcement (i.e., August 2000) can enjoy a seven-year income tax holiday. After that date, the income tax holiday will be five years, in line with the new policy announcement.
- The 58 provinces of Zone 3 will be divided into two areas, based on each province's stage of development. New projects in Zone 3 will no longer be eligible for a 75 percent reduction of import duty on raw materials used for domestic sales.
- More developed provinces (40):

Inside Industrial Estates – For projects submitted before December 30, 2004, and that locate in industrial estates that were approved by BOI before August 2000, there will be no change from the current Zone 3 incentive scheme. Projects submitted after December 30, 2004, will no longer be eligible to receive a 25 percent reduction in the project's infrastructure costs from net profits.

Outside Industrial Estates – New projects will receive an eight-year income tax holiday, with no additional income tax reduction, and a 25 percent reduction in the project's infrastructure costs from net profits.

Less-developed provinces (18):

There will be no change from the current Zone 3 incentive scheme for new projects in the less-developed provinces (see list above).

Complete information on BOI policies, programs, incentives, and application procedures can be found on the BOI website at www.boi.go.th.

RIGHT TO PRIVATE OWNERSHIP AND ESTABLISHMENT

Private entities may establish and own business enterprises. The principal forms of business organization under Thai law are sole proprietorships, partnerships, limited

companies, and public limited companies. In addition, branches of foreign corporations are recognized, and a "representative" or "liaison" office of a foreign company may receive special recognition. Regardless of the form of business entity, most businesses must apply for business registration. Establishment of a business in certain sectors by a foreign entity may be restricted by the Alien Business Law, or may not benefit from the Treaty of Amity as discussed above.

A Thai private limited company is similar to a corporation in the United States, and may be wholly owned by a foreigner unless the corporation is involved in a business activity reserved for Thai nationals. A public limited company is allowed to offer its shares to the public. Eight laws pertaining to individual industries limit foreign ownership of companies listed on the Stock Exchange of Thailand.

PROTECTION OF PROPERTY RIGHTS

Rights in property are guaranteed by the Constitution against condemnation or nationalization without fair compensation. Secured interests in property are recognized and enforced.

Thailand has a civil law system under which all laws are embodied in statutes or codes promulgated by the government. This practice is in contrast to the common law system in many Western countries, where court interpretations of statutes serve as governing legal precedent.

There is an independent judiciary that provides a forum for fair settlement of disputes. A great deal of status is attached to being a judge, and the examinations to enter the judiciary are very difficult. The judiciary jealously guards its independence.

Agencies of the government, as parties to commercial contracts, may be sued in the courts, and cannot raise a defense of sovereign immunity. However, state property is not subject to execution.

There are four basic codes: Civil and Commercial Code, Criminal Code, Civil Procedure Code, and Criminal Procedure Code. In adopting these codes early in the twentieth century, Thailand selected features of the two major western legal systems (common law and civil law), and adapted to circumstances in Thailand provisions drawn from Britain, Germany, Switzerland, France, Japan, Italy, India, and other foreign systems. Decisions and rulings of the judiciary and civil service can have considerable force as precedents.

There are three levels to the judicial system in Thailand: the Court of First Instance, which handles most matters at inception, the Court of Appeals, and the Supreme Court. There are specialized courts such as the Labor Court, Family Court, Tax Court and the recently established Intellectual Property and International Trade Court and Bankruptcy Court.

INTELLECTUAL PROPERTY PROTECTION

Despite the passage of significant Intellectual Property Rights (IPR) legislation and a good working relationship between foreign business entities and Thai enforcement authorities, IPR piracy continues at high levels. U.S. copyright industries reported an estimated annual trade loss of more than USD 200 million from IPR infringement in 2000. Since November 1994, Thailand has been on the U.S. Special 301 "Watch List". In July 2001, the Prime Minister appointed the Minister of Interior to head a joint interagency and private sector committee to improve IPR protection.

Obstacles to effective IPR enforcement are numerous. Resource limitations, especially in the wake of the financial crisis, hamstring police capabilities and judicial administration alike. Irregularities in police and public prosecutor procedures occasionally have resulted in the substitution of insignificant defendants for major ones and the disappearance of vital evidence. The frequency of raids compromised by leaks from police sources has declined, but remains a concern. Pirates, including those associated with transnational crime syndicates, have responded to stepped-up levels of enforcement with intimidation against rights-holders' representatives.

A specialized intellectual property court established in 1997 has improved judicial procedures and imposed higher fines. Criminal cases generally are disposed of within six to twelve months from the time of a raid to the rendering of a conviction, and conviction rates are very high. In many cases, penalties imposed are insufficient deterrence, according to rights-holders; however, a growing number of people are serving time in jail for IPR violations. Effective prosecutions can be labor-intensive for rights-holders, who often investigate, participate in raids, help coordinate the warehousing of confiscated property, and assist in the preparation of documentation for prosecution.

Amendments to Thailand's patent regime, which were designed to meet Thailand's TRIPs obligations, entered into effect in September 1999. However, Thailand's under-funded patent office lacks the sufficient number and expertise of patent examiners to keep up with its volume of applications. Amendments to the Thai Food and Drug Administration's safety monitoring program for new pharmaceutical products raise data protection concerns.

Thailand's copyright law became effective in March 1995, bringing Thailand into closer conformity with international standards under TRIPs and the Berne Convention. With active participation on the part of U.S. industry associations, the Thai police conducted many more raids on copyright infringement operations in 2000 than in previous years, both at the retail and production levels. Nevertheless, the scale of the problem is growing. A draft Optical Disk Plant Control Act under consideration in the parliament is designed to enhance the authority and capabilities of the police to act against operators of illicit optical disk factories.

The government streamlined trademark application procedures pursuant to the IPR action plan in 1998. Additional amendments enacted in June 2000 broadened the

legal definition of a mark and were designed to bring Thailand's trademark law in compliance with the TRIPs agreement. While these developments have created a viable legal framework and have led to some improvements in enforcement, trademark infringement remains a serious problem. U.S. companies with an established presence in Thailand and a record of sustained cooperation with Thai law enforcement officials have had some success in defending trademarks, but the process remains time-consuming and expensive.

TRANSPARENCY OF THE REGULATORY SYSTEM

In 1999, Thailand enacted a new Trade Competition Act intended to strengthen the government's ability to regulate price fixing and market monopolies. The law established a Trade Competition Commission with the authority to place limitations on market share and revenues of firms with substantial control of individual market sectors, to block mergers and other forms of business combinations and to levy fines for price fixing and other proscribed activities. The government continues to have the authority to control the price of specific products under the recently revised Goods and Services Price Act of 1999. In practice, very few commodities are subject to formal price controls. However, the government does use its control of major suppliers of products and services such as Thai Airways and PTT (oil and gas) to influence prices in the market.

Thailand has extensive legislation aimed at the protection of the environment, including the National Environmental Quality Act, the Hazardous Substances Act, and the Factories Act. Food purity and drug efficacy are controlled and regulated by a Food and Drug Administration with authority similar to its U.S. counterpart. Likewise, labor and employment standards are set and regulated by the Ministry of Labor.

Despite the good intentions of most regulatory regimes, consistent and predictable enforcement of government regulations remains an obstacle to investment in Thailand. Gratuity payment to civil servants responsible for regulatory oversight and enforcement unfortunately remains a common practice. Through such payments, regulations can often be by-passed or ignored and approval processes expedited. Firms that refuse to make such payments can be placed at a competitive disadvantage when compared to other firms in the same field. However, most observers believe that the overall trend in this respect is positive, especially in foreign-owned businesses.

EFFICIENT CAPITAL MARKETS AND PORTFOLIO INVESTMENT

The Thai government maintains a regulatory framework that broadly encourages investment and largely avoids market-distorting support for specific sectors. Government policies do not restrict the free flow of financial resources to support product and factor markets, and credit is generally allocated on market terms rather than by "directed lending". Legal, regulatory, and accounting systems are largely transparent. The Thai government has devoted considerable effort to bringing these systems into line with international norms, and significant progress has been made. However, much remains to

be done to implement legal and regulatory changes and human resources constraints will limit overall progress in some areas, particularly auditing, for the foreseeable future.

Foreign investors are not restricted from borrowing on the local market, but there are a number of regulations that affect foreign portfolio investment. Thailand maintains regulatory maximum foreign ownership limits, and shares of listed companies are traded on both a domestic and alien (or foreign) board to enable authorities to track foreign ownership. Limits on foreign ownership of Thai companies are perhaps most prominent in the financial sector. Even so, foreign investors may now hold more than 49 percent (up to 100 percent) of the shares of Thai financial institutions for a period of ten years, and limits on foreign ownership are generally being relaxed as Thailand liberalizes in an attempt to attract additional foreign investment.

In theory, the private sector has access to a wide variety of credit instruments, ranging from fixed term lending to overdraft protection to bills of exchange and bonds. In fact, however, private debt markets are not well-developed, and most corporate financing, whether for short-term working capital needs, trade financing or project financing, is commercial bank/finance company borrowing.

Access to credit is a major issue in the aftermath of the financial crisis that began in Thailand in mid-1997. Insolvency led the Thai government to close 56 finance companies in December 1997. The uncertain economic outlook and a portfolio of non-performing loans that would reach 47 percent of total loans by mid-1999 has led banks to approach new lending extremely cautiously. Despite the government's successful efforts to bring down interest rates and stimulate economic growth, lending has still not picked up. As of May 2001, total commercial bank credits were 9.1 percent below their level of a year earlier. After factoring in write-offs of outstanding debt and loans transferred to asset management companies (AMCs), commercial bank credits are down 0.2 percent from 2000 levels.

Restoring the health of the banking system is a major government focus. On August 14, 1998, the Bank of Thailand and Ministry of Finance announced a major program to assist financial institutions to recapitalize. Under the program, the Ministry of Finance will provide recapitalization assistance if financial institutions meet certain conditions, designed to ensure that banks raise capital on their own and that existing shareholders bear losses on the existing portfolio, while rewarding new lending and corporate debt restructuring. The scheme has attracted only moderate usage, due to its strict conditions, but financial institutions in general have been relatively successful in raising capital on their own. Since January 1998, private commercial banks have raised over 447.4 billion Baht (USD 11.42 billion) on the market, and finance companies have raised nearly 67.5 billion Baht (USD 1.72 billion). Financial institutions were required to meet gradually-increasing provisioning requirements through December 31, 2000. By July 31, 2000, financial institutions agreed with the Bank of Thailand on how they would meet the December 31, 2000 provisioning requirements.

The financial sector has also undergone significant restructuring in the aftermath of the crisis. In addition to the 56 finance companies closed in 1997, the government has also intervened and taken over seven commercial banks, which have now been recapitalized through the conversions of debt held by the Bank of Thailand's Financial Institutions Development Fund (FIDF) into equity. One of these banks was closed, two were merged with other financial institutions, and two have been privatized, with two more scheduled for sale.

The overall health of the banking sector is affected by the high levels of non-performing loans (NPLs) banks are carrying on their books. After peaking at 47 percent of total lending in May 1999, NPLs slowly declined to stand at 17.6 percent of total lending by April 2001. The figure may actually approach 30 percent, however, if non-performing loans transferred to banks' private asset management companies are taken into account. The level of NPLs will decline further with debt restructuring, but progress has been slow. As NPL levels fall, however, banks' provisioning requirements will also fall, thus benefiting bottom lines in the sector.

One of the main pillars of the Thaksin government's financial reform plan is the Thai Asset Management Corporation (TAMC), which will take over 1.37 trillion Baht (USD 30 billion) in bad loans from local financial institutions and asset management companies by the end of 2001. Following passage of the TAMC's legal framework in June 2001, TAMC operations are expected to begin in the third quarter. The TAMC will have broad powers to expedite debt restructuring and press borrowers to the negotiating table.

A total of 112,500 NPLs will be transferred to the TAMC – 110,000 from state-owned financial institutions and asset management companies, and the remainder from private banks. Of the 1.37 trillion Baht (USD 30 billion) in bad loans to be handled by the TAMC, only around 250 billion Baht (USD 5.5 billion) will come from private banks. Assets will be transferred at collateral value (excluding personal guarantee), with payment coming in the form of ten-year non-negotiable bonds issued by the TAMC and guaranteed by the FIDF. Interest paid by the bonds will be tied to average deposit rates quoted by Thailand's five largest banks.

The Bank of Thailand had sole responsibility for selecting financial institution and asset management company assets for transfer to the TAMC. Qualified assets must involve outstanding debt of at least five million Baht (USD 110,000), must have some form of collateral, must involve borrowers with two or more creditors, and must not be subject to an interim or final receiving order of the Bankruptcy Court. The TAMC is only authorized to take over assets that were classified as NPLs as of December 31, 2000. In addition, state-owned financial institutions and asset management companies are required to transfer all qualified assets to the TAMC, while private financial institutions and asset management companies may transfer assets on a voluntary basis. To prevent creditor disagreements from impeding restructuring under the BOT's Corporate Debt Restructuring Advisory Committee (CDRAC), however, the TAMC law will force financial institutions to consent to the transfer of qualified assets. Assets must either be

transferred in their entirety or not at all, and banks choosing not to participate face an immediate BOT examination of their assets, loan collateral, and provisioning funds.

Financial institutions and asset management companies will follow a set formula in splitting future profits and losses on assets transferred to the TAMC. The first portion of any loss, up to 20 percent of the NPL's total collateral value, will be absorbed by the financial institution or asset management company. The next 20 percent of any loss will be split evenly between the financial institution or asset management company and the TAMC, and the remainder will be absorbed entirely by the TAMC. While most financial institutions concede that pooling bad loans together into a single workout agency should accelerate restructuring, questions remain over the agency's operations, transparency, and management. The TAMC is only authorized to take over assets that were classified as NPLs as of December 31, 2000. Given the ongoing economic slowdown, however, several financial institutions have expressed concern about a possible increase in NPLs later in 2001.

Thai firms appear to employ few defenses against foreign investment, especially through cross- and stable-shareholding arrangements. Furthermore, defenses against hostile takeovers would typically be applied against all potential investors rather than against foreign potential investors alone. Companies are not forbidden from specifying limits on foreign ownership more strict than those established by the government, but the practice is not considered prevalent. In the current environment, limits on foreign ownership and participation in the Thai economy have eased, a trend that should continue.

POLITICAL VIOLENCE

In recent years Thailand has developed a much more stable and transparent political system, although in the past there were frequent changes in government, often by military intervention. The last coup was in 1991, followed in 1992 by political unrest and a confrontation in the streets of Bangkok in which over fifty civilian demonstrators were killed. The "May 1992 events" were a real shock to the Thai political system and stimulated a remarkable democratic recovery. Since 1992, the military has not interfered in the operation of the civilian government, and this appears likely to remain the case for the foreseeable future. There have been four successful elections (1992, 1995, 1996, and 2001), as well as a change of government in 1997 and 2001. A non-partisan assembly rewrote the nation's constitution, which was put into force in October 1997. One of the main reforms of the new constitution is the establishment of three independent agencies: the Election Commission, the National Counter Corruption Commission, and the Constitutional Court. Each of these new bodies is expected to play a key role in screening qualified candidates and thereby reducing vote-buying by candidates for the national parliament. Vote-buying persisted as a problem during the January 2001 election, however.

CORRUPTION

Thailand has laws to combat corruption, and the independent National Counter Corruption Commission coordinates official investigations into corruption. However, there are regular allegations of improper conduct, both in the Thai press and anecdotally in the business community. American executives with long experience in Thailand advise new-to-market companies that it is far easier to avoid getting started with corrupt transactions than to stop such practices once a company has been identified as willing to operate in this fashion. American firms that operate under the strict guidelines of the Foreign Corrupt Practices Act are able to compete successfully in Thailand.

Despite recent improvements, both foreign and Thai companies continue to complain about irregularities in the Thai Customs Service. Recent Thai administrations have stated publicly their intention to improve transparency in the evaluation of bids and the awarding of contracts. Increasing media scrutiny of public figures has raised political pressure to curtail favoritism and corruption. Nonetheless, the press features frequent allegations of irregularities in public contracts, most notably over the use of public lands, as well as charges of favoritism in government tendering practices, e.g., revising tender requirements so that a preferred company wins over its competitors.

In its 2001 ranking of corrupt practices, Transparency International ranked Thailand along with Malawi at 61st (of a total of 91 ranks) on its corruption perception index (the higher the number, the worse the corruption). According to some studies, a cultural propensity to forgive bribes as a normal part of doing business and to equate cash payments with finders fees or consultants' charges, coupled with the low salaries of civil servants, encourages officials to accept illegal inducements.

BILATERAL INVESTMENT AGREEMENTS

The U.S.-Thai Treaty of Amity and Economic Relations of 1966, discussed above, allows U.S. citizens and businesses incorporated in the U.S. or in Thailand that are majority owned by U.S. citizens to engage in business on the same basis as Thais, exempting them from most of the restrictions on foreign investment imposed by the Alien Business decree of 1972. Under the Treaty, Thailand is permitted to apply restrictions to American investment only in the fields of communications, transport, banking, the exploitation of land or other natural resources, and domestic trade in agricultural products.

Thailand also has bilateral investment agreements with 25 countries, such as Germany, the Netherlands, the United Kingdom, China, and members of the Association of South East Asian Nations (ASEAN). These agreements establish guidelines for expropriation compensation and the repatriation of capital, but do not include national treatment provisions.

OPIC AND OTHER INVESTMENT INSURANCE PROGRAMS

The Overseas Private Investment Corporation (OPIC) is open for business in Thailand. The agency is currently involved with several power generation projects being developed as part of the Thai government's Independent Power Producer Scheme. For example, OPIC is currently helping U.S. firms build a 700 Megawatt gas-powered plant by underwriting USD 185.7 million in political risk insurance that covers, for the first time, interest rate swaps. Edison Mission Energy and Texaco are the equity investors in the project. Citibank and Bank of America are providing financing. Thailand became a member of the Multilateral Investment Guarantee Agency (MIGA) in October 2000.

LABOR

According to a February 2001 Labor Force Survey (LFS) conducted by the National Statistics Office, Thailand has a labor force of 33.2 million workers out of a total population of 62.8 million. This figure includes all Thai fifteen years of age or older who are actively seeking work.

The unemployment rate was 4.8 percent during the first quarter of 2001, versus a rate of 4.3 percent during the same period in 2000. The rising unemployment rate stems from ongoing economic fragility in the wake of the 1997 financial crisis. Reduced access to capital has led to employment freezes in many sectors, while Thai affiliates of some multinationals have laid off employees as part of broader corporate restructuring plans. The Thai government's decision not to forcibly repatriate large numbers of foreign workers in the fisheries, construction, and other semi-skilled sectors may also have affected employment levels. Finally, sluggish private investment has contributed to employment declines, especially in the construction sector.

Despite past rapid growth in the industrial and service sectors, 36.1 percent of the Thai labor force is still employed in the agricultural sector. However, the shift of workers from agriculture is continuing, especially in the Northeast where agricultural productivity and investment are lower. As a consequence, recent years have seen a constant flow of rural, generally unskilled Thais seeking work in Bangkok and the more industrialized regions, both seasonally and on a permanent basis. This ready availability of migrant labor contributed to Thailand's rapid industrial growth through the mid-1990s, particularly in the light manufacturing and construction sectors.

The economic downturn stemmed shortages in the labor market of workers with at least a secondary education. As Thailand's economy recovers, however, it is likely that highly skilled and experienced engineers, technicians and managers will again be in short supply. In the past, many multinational firms brought in expatriate professionals because qualified local personnel simply were not available, even at high salaries. Finding, training, and retaining qualified employees to work in the manufacturing facilities being developed in industrial estates, such as those along the Eastern Seaboard, will continue to be a challenging government priority.

Thailand's education system is still geared toward the needs of a largely agrarian, traditional economy and society and lags behind the country's contemporary skills requirements. The government has made great progress over the last two decades in providing basic education. Thailand's gross primary school enrollment in 2000 was 91.5 percent, and the adult literacy rate in 2000 was 94.0 percent, one of the best in the region. In 2000, Thailand had 513,255 students enrolled in public and private colleges and universities.

An integral part of Thailand's educational reform program, the country's first National Education Act was promulgated in August 1999. The Act stipulates the right of all Thai citizens to receive free basic public education for at least twelve years, and raised the level of compulsory education from six to nine years. Pursuant to the 1999 Act, the free basic education and compulsory education provisions will take effect from August 20, 2002. Children are required to enroll in a basic education institution from the age of seven, and must remain in the educational system through the age of sixteen.

All employers must define the terms of employment for their staff, and employers with ten or more employees are required to specify working regulations. A new labor law enacted in late 1998 brought labor practices more in line with International Labor Organization (ILO) standards. The law cut the work week to a maximum of forty-eight hours including overtime for all types of work, with overtime payable at one and one-half times the hourly rate. Hazardous work may not exceed seven hours per day or forty hours per week. All employees are entitled to a vacation of six workdays a year, in addition to thirteen holidays traditionally observed in Thailand. Under the labor law, the employment of children under the age of fifteen is prohibited, and there are restrictions on the employment of children and youths through the age of eighteen.

Thailand's "social safety net" is considered inadequate by industrialized-country standards. The social security system consists of two systems. The Workmen's Compensation Act of 1994 requires employers with ten or more employees to contribute yearly 0.2-1.0 percent of the employee's earnings to the Workmen's Compensation Fund. The Fund provides benefits to employees who are injured, sick, disabled or die from work-related injury. The Social Security Act has been in effect since 1990. This Act covers enterprises with ten or more employees. Contributions to the Social Security Fund from the government, the employer, and the employee are mandated. The Social Security Fund provides compensation to insured workers under six categories: injury or sickness, child delivery, crippling injury, death, child welfare, and old age. In the first four categories, each party contributes 1.5 percent of the wages of the insured. For child welfare and old age cases, three percent is contributed. Currently, the Social Security Fund does not cover unemployment compensation. In practice, disbursement of unemployment benefits is dependent on the state of the economy and the government's financial resources.

The labor relations climate in Thailand is generally peaceful, with strikes relatively infrequent. Less than two percent of the total labor force is unionized; about ten percent of the industrial work force is organized. In 2000, the union rights of state

enterprise workers were successfully restored after having been abolished in the wake of a 1991 military coup. The State Enterprise Labor Relations Act (SELRA) was reaffirmed by the Thai Parliament and became law on April 8, 2000. State enterprise labor unions recently completed a re-certification process and elected new union leaders.

FOREIGN TRADE ZONES/FREE PORTS

Thailand has ten export processing zones to which businesses may import raw materials and export finished products free of duty. These zones are located within industrial estates, and many have customs facilities to speed processing. In addition to these zones, factories may apply for permission to establish a bonded warehouse within their premises to which raw materials, used exclusively in the production of products for export, may be imported duty free.

The Industrial Estate Authority of Thailand (IEAT) established the first industrial estates in Thailand, including Laem Chabang Industrial Estate in Chonburi Province and Map Ta Phut Industrial State in Rayong Province. More recently, private developers have become heavily involved in the business. The IEAT operates nine estates, plus 22 more jointly with the private sector. There are 54 industrial estates operated by private sector developers. Most of these have received promotion privileges from the Board of Investment.

FOREIGN DIRECT INVESTMENT STATISTICS

All statistics are provided by the Thai government's Board of Investment (BOI). Foreign direct investment (FDI), including inflows for bank recapitalization, totaled 99.4 billion Baht (USD 2.5 billion) in 2000, compared with 134.6 billion Baht (USD 3.6 billion) in 1999. Major FDI recipients included the services (USD 752 million) and chemicals (USD 551 million) sectors.

In 2000, the U.S. was the largest source of FDI with USD 871 million, followed by Japan with USD 585 million. There are no reliable local statistics available for cumulative investment by country of origin. The Embassy estimates the total present value of U.S. investment in Thailand to be in excess of USD 16 billion.

In 2000, major U.S. investment projects approved by the BOI include the following (note that a U.S. investment is classified as any investment with at least ten percent U.S. capital):

- Procter and Gamble (personal care products)
- Lucent Technologies Microelectronics (integrated circuits)
- Alphatec Semiconductor Packaging (integrated circuits)
- Parish Structural Products (surglass frame)
- Johnson and Johnson (personal care products)
- PCTT (circuit boards)
- Safeskin Medical and Scientific (rubber gloves)

- Pacific Millennium Paper and Packaging (corrugated boxes)
- Kellogg (Rice Krispies Treats)

Table 1

**Net Flow of Foreign Investment (excluding bank recapitalization)
By Country of Origin in USD millions**

	CY1999	CY2000
Japan	490	585
U.S.A	638	871
Canada	3	5
Hong Kong	234	318
Taiwan	121	188
Switzerland	60	-5
Australia	13	20
South Korea	5	-5
China	-2	6
ASEAN:	571	294
Singapore	530	265
Malaysia	28	18
Indonesia	1	1
Philippines	3	0
EU:	1,373	414
U.K	185	444
Germany	290	64
France	237	7
Netherlands	650	118
Belgium	-36	-25
TOTAL	3,557	2475

Table 2

**Net Foreign Direct Investment in USD Millions
By Sectors**

	CY 1999	CY2000
1. Financial Institutions	244	99
2. Trade	1,041	50
3. Construction	-155	-19
4. Mining & Quarrying	-42	-313
5. Agriculture	2	1
6. Industry	1,267	1,954
1.1 Food and Sugar	93	164
1.2 Textiles	20	0
1.3 Metal & Non-Metalic	261	-70

	<u>CY 1999</u>	<u>CY2000</u>
1.4 Electrical Appliances	435	491
1.5 Machinery and Transport Equipment	388	549
1.6 Chemicals	6	551
1.7 Petroleum Products	8	41
1.8 Construction Materials	37	55
1.9 Others	18	174
7. Services	481	752
8. Real Estate	150	70
9. Others	569	-117
TOTAL FDI	3,557	2,475

Source: Bank of Thailand

Table 3
Thai Direct Investment Abroad
In USD Millions

	<u>CY1999</u>	<u>CY2000</u>
	-338	-60

Source: Bank of Thailand

Table 4
Portfolio Investment Flows
In USD Millions

	<u>CY1999</u>	<u>CY2000</u>
TOTAL		
Equity Securities	946	887
Debt Securities	-555	-555

Source: Bank of Thailand

Table 5
Foreign Investment through Board of Investment by Number and Value in USD Millions By Country of Origin and Applications Approved

	<u>CY1999</u>		<u>CY2000</u>	
	Number	Value	Number	Value
Japan	188	715	282	2,674
U.S.A	53	1,225	72	940
Canada	3	687	6	27
Asian NIEs				
Taiwan	86	209	120	439
Hong Kong	25	50	31	155
Korea	19	26	17	35
Singapore	52	185	84	496
China	7	15	8	9

	<u>CY1999</u>		<u>CY2000</u>	
Malaysia	27	90	43	152
Indonesia	5	30	4	32
Philippines	1	2	0	0
India	6	36	11	253
EU	73	963	134	716
UK	17	104	38	145
Germany	12	49	39	159
Switzerland	10	84	10	57
France	11	75	13	27
Belgium	7	23	2	8
Italy	3	3	9	11
Netherlands	18	594	21	158
Australia	10	31	21	67
TOTAL	517	3,596	761	5,295

Source: Board of Investment

Table 6
Start Up Operations

	<u>CY 1999</u>		<u>CY 2000</u>	
Japan	177	2,351	184	2,381
U.S.A.	21	270	38	424
Canada	0	0	1	0.3
Asian NIEs				
Taiwan	27	79	45	393
Hong Kong	10	20	14	520
Korea	11	91	15	63
Singapore	36	193	38	763
China	1	4	5	13
Malaysia	11	28	6	16
Indonesia	1	2	1	2
Philippines	1	2	0	0
India	2	3	2	3
EU	55	645	70	1,107
UK	12	54	19	542
Germany	16	52	11	45
Switzerland	2	2	8	61
France	4	59	10	48
Belgium	3	2	5	26
Italy	0	0	0	0
Netherlands	12	110	17	616
Australia	8	202	9	35
TOTAL	346	3,831	427	6,054

Source: Board of Investment

This report was prepared by the Economic Section (U.S. Department of State) at U.S. Embassy Bangkok. For further information, contact the Economic Section at tel.: (66) (2)205-4995, fax: (66) (2) 254-2839.